

severed from the portion of the contract relating to the five aircraft. Assume also that under all the facts and circumstances it is determined that the five aircraft represent the primary subject matter of the contract, and that the spare and replacement parts do not represent the primary subject matter of the contract. In 1984, X tenders the five aircraft and seven of the spare and replacement parts to Y. Y accepts the aircraft and the parts subject to X's delivery of the balance of the spare and replacement parts. For Federal income tax purposes the contract is deemed to have been completed in 1984. Accordingly, X must include in gross income in 1984 the entire contract price, less the portion of the gross contract price reasonably allocable (if any) to the parts not delivered in 1984. X must deduct from gross income in 1984 the entire costs properly allocable to the contract, less the entire costs incurred that are properly allocable to the parts not delivered in 1984. X will account for the income and costs allocable to the parts not delivered in 1984 under a proper method of accounting.

(iii) *Contingent compensation.* In the case of a long-term contract, "final completion and acceptance" shall be determined without regard to any term of the contract providing for additional compensation contingent upon the continued successful performance of the subject matter of the contract after the subject matter of the contract has been accepted by the purchaser (such as an incentive fee payable if a satellite remains in operation after it is placed in orbit). Such contingent compensation shall be included in gross income in the appropriate taxable year determined under the taxpayer's method of accounting other than a long-term contract method.

(iv) *Certain supervision of installation.* In the case of a long-term contract, "final completion and acceptance" shall be determined without regard to any obligation on the part of the contractor to assist or to supervise installation or assembly of the subject matter of the contract where such installation or assembly is to be performed by the purchaser and, under applicable contract law, the subject matter of the contract may be accepted by the purchaser prior to such installation or assembly. If the preceding sentence applies to a contract, "final completion and acceptance" shall be determined without regard to such obligation [.] In addition, the entire gross contract price less the portion of the gross con-

tract price (if any) reasonably allocable to such obligation, shall be included in gross income in the taxable year in which the contract is completed[.] Further, all costs properly allocable to the contract and which have been incurred prior to the end of the taxable year in which such contract is completed shall be deducted in such year[.] Finally, all other costs properly allocable to such contract and the portion of the gross contract price reasonably allocable to the obligation to assist or to supervise installation shall be accounted for under a proper method of accounting other than a long-term contract method.

(v) *Subcontractors.* In the case of a subcontractor who completes work on a long-term contract prior to the completion of the entire contract, "final completion and acceptance" of the contract with respect to such subcontractor shall be deemed to have occurred when the subcontractor's work has been completed and has been accepted by the party with whom the subcontractor has contracted.

(vi) *Disputes.* Completion of a long-term contract is determined without regard to whether a dispute exists at the time the taxpayer tenders the subject matter of the contract to the party with whom the taxpayer has contracted. See paragraphs (d)(2), (3) and (4) of this section.

(3) *Extended period long-term contract*—(i) *General Rule.* This paragraph (b)(3) does not apply to contracts accounted for under the percentage of completion method. Except as provided in paragraph (b)(3)(ii) of this section, the term "extended period long-term contract" means any long-term contract that the taxpayer estimates (at the time such contract is entered into) will not be completed (as defined in paragraph (b)(2) of this section) within the 2-year period beginning on the first date (hereinafter, "the contract commencement date") that the taxpayer incurs any costs (other than costs such as bidding expenses, or expenses incurred in connection with negotiating the contract) allocable to such contract (under the cost allocation rules of paragraph (d)(6) of this section). The preceding sentence shall be applied without regard to when costs allocable